

Issue: Responsible Corp. Officer - Failure to File or Pay Tax

A hearing was held on December 16, 1996. Upon consideration of all the evidence, it is recommended that this matter be resolved in favor of the taxpayer.

Findings of Fact:

1. The Department's *prima facie* case was established by the admission into evidence of the Notice of Penalty Liability ("NPL") and the Notice of Deficiency ("NOD"). The NPL dated September 22, 1994, reflects a total liability due and owing in the amount of \$43,206.79 for the period June 1992 through March 1993. Dept. Ex. No. 1. The NOD dated December 23, 1994 reflects a total liability in the amount of \$3,493.11 for the first and second quarters of 1992 and the first quarter of 1993. Dept. Ex. No. 2.

2. TAXPAYER, TAXPAYER A and TAXPAYER A's father, TAXPAYER B formed CORPORATION in 1988. Tr. pp. 28, 29.

3. TAXPAYER A and TAXPAYER B hired personnel for the company. Tr. p. 31; Taxpayer Ex. No. 1.

4. TAXPAYER B's personal accountant handled the corporation's books and records. Tr. p. 31.

5. TAXPAYER A and TAXPAYER had signatory authority on the corporate bank account. Tr. p. 45; Dept. Grp. Ex. No. 3.

6. TAXPAYER was the Secretary and Vice-President of CORPORATION and owned 40% of the company's stock. Tr. p. 45. TAXPAYER A was the President and also a 40% shareholder. Dept. Ex. No. 4. Taxpayer's responsibilities included customer sales and product design. Tr. pp. 23, 24, 29. TAXPAYER A and TAXPAYER B handled the company's financial and tax obligations. Tr. pp. 29, 30. Taxpayer received \$50,000 in salary in 1992. Tr. p. 46.

7. In 1992, the company experienced financial difficulties and TAXPAYER B loaned the company \$100,000 and thereafter owned a percentage of the company.

Subsequent to the loan, he became more actively involved in the business, (Tr. p. 29), and later loaned additional monies to the company. Tr. p. 30.

8. Under the November 16, 1992 agreement between CORPORATION and TAXPAYER B, both TAXPAYER and TAXPAYER A gave voting proxies to TAXPAYER B. Tr. p. 40. Taxpayer Ex. No. 2.

9. Taxpayer signed the second quarter 1992 withholding tax return and the July and November 1992 sales tax return. Tr. p. 46; Dept. Ex. No. 5.

10. TAXPAYER resigned his position with CORPORATION on March 31, 1993. Tr. pp. 46, 47.

Conclusions of Law:

The Department seeks to impose personal liability on TAXPAYER pursuant to Section 1002(d) of the Illinois Income Tax Act which provides:

Any person required to collect, truthfully account for, and pay over the tax imposed by this Act who willfully fails to collect such tax or truthfully account for and pay over such tax or willfully attempts in any manner to evade or defeat the tax or the payment thereof, shall, in addition to other penalties provided by law, be liable to a penalty equal to the amount of the tax evaded, or not collected, or not accounted for and paid over

35 **ILCS** 5/1002(d) (*formerly* Ill. Rev. Stat. 1991, ch. 120, 10-1002(d)).¹

Further, the Department also seeks to impose liability upon taxpayer pursuant to Section 13 1/2 of the Retailers' Occupation Tax Act (ROTA). Section 13 1/2 is modeled after Section 6672 of the Internal Revenue Code, which imposes liability upon those individual persons actually responsible for an employer's failure to withhold and pay over the taxes. See, Branson v. Department of Revenue, 168 Ill. 2d 247 (1995); Department of Revenue v. Heartland Investments, Inc., 106 Ill. 2d 19 (1985). While the Branson decision addressed a situation in which the Retailers' Occupation Tax was applicable, a comparison of the

¹. The Uniform Penalty and Interest Act, 35 **ILCS** 735/3-7, which provides for a personal liability penalty, is effective for taxes incurred as of January 1, 1994.

Illinois Income Tax provision reveals that the same elements of responsibility and willfulness are adopted and thus a similar analysis is required.

In determining whether an individual is a responsible person the courts have indicated that the focus should be on whether that person has significant control over the business affairs of a corporation and whether he or she participates in decisions regarding the payment of creditors and the disbursal of funds. See, e.g. Monday v. United States, 421 F.2d 1210 (7th Cir. 1970), cert. denied 400 U.S. 821 (1970). Liability attaches to those with the power and responsibility within the corporate structure for seeing that the taxes are remitted to the government. *Id.*

Although TAXPAYER worked at the business daily, his responsibilities were limited to customer sales and product design. Credible testimony was given by both TAXPAYER and other company salesmen that the taxpayer spent all of his time out on the sales floor and did not actively participate in CORPORATION's financial decisions. Authorization of material purchases was given by TAXPAYER B. It was also TAXPAYER B who prepared the payment checks and handled accounts receivable collections. TAXPAYER A handled the company payroll and distributed the checks. Thus, it appears that responsibility for the financial workings of the company lay with TAXPAYER A and TAXPAYER B.

Taxpayer had signatory authority on the corporation's bank account, however, he does not appear to have had a role in decisions regarding the payment of creditors. Taxpayer did not hire and fire personnel for the company. It is quite conceivable that TAXPAYER was occupied with customer sales from the store's opening to the end of the business day. Taxpayer did sign three returns during the audit period, however, this was done for convenience when TAXPAYER A was out of the office. Taxpayer did not take any part in the preparation of the tax returns, nor did he normally sign the return or the check. In fact, the record does not reflect that taxpayer actively wrote checks for any corporate expenses during the audit period.

Based on the foregoing, I believe that the taxpayer did not have sufficient control over the corporation's finances to establish him as a responsible party, and has presented sufficient evidence to rebut the Department's *prima facie* case.

WHEREFORE, for the reasons stated above, it is my recommendation the Notice of Deficiency and the Notice of Penalty Liability be cancelled.

Christine O'Donoghue
Administrative Law Judge